



California Fair Political Practices Commission

November 8, 1985

Richard E. Winnie
City Attorney
City of Oakland
City Hall, One City Hall Plaza
Oakland, CA 94612

Re: Your Request for Assistance
Our File No. A-85-228

Dear Mr. Winnie:

You have asked for the "legal authority" behind the Commission's position that a client of a law firm is a "source of income," within the meaning of Government Code Section 87103(c), to an owner of 10 percent or more of the law firm when that owner's pro rata share of the fees paid to the law firm exceeds \$250. You have also requested a meeting with the Commission's legal staff in order to review guidelines which you have prepared for your councilmembers. We would be pleased to meet with you to discuss the guidelines.

The Political Reform Act (the "Act")^{1/} requires that a public official disqualify himself or herself from any decision in which he or she knows or has reason to know that he or she has a financial interest. Section 87100. Section 87103 (as amended by Chap. 611, Stats. 1985) defines when an official has a financial interest in a decision.

An official has a financial interest in a decision within the meaning of Section 87100 if it is reasonably foreseeable that the decision will have a material financial effect, distinguishable from its effect on the public generally, on the official or a member of his or her immediate family or on:

^{1/} Government Code Sections 81000-91015. All statutory references are to the Government Code unless otherwise indicated.

(a) Any business entity in which the public official has a direct or indirect investment worth one thousand dollars (\$1,000) or more.

(b) Any real property in which the public official has a direct or indirect interest worth one thousand dollars (\$1,000) or more.

(c) Any source of income, other than gifts and other than loans by a commercial lending institution in the regular course of business on terms available to the public without regard to official status, aggregating two hundred fifty dollars (\$250) or more in value provided to, received by or promised to the public official within 12 months prior to the time when the decision is made.

(d) Any business entity in which the public official is a director, officer, partner, trustee, employee, or holds any position of management.

(e) Any donor of, or any intermediary or agent for a donor of, a gift or gifts aggregating two hundred fifty dollars (\$250) or more in value provided to, received by, or promised to the public official within 12 months prior to the time when the decision is made.

For purposes of this section, indirect investment or interest means any investment or interest owned by the spouse or dependent child of a public official, by an agent on behalf of a public official, or by a business entity or trust in which the official, the official's agents, spouse, and dependent children own directly, indirectly, or beneficially a 10-percent interest or greater.

Section 87103.

As can be seen, an official must disqualify himself or herself if the decision will affect his or her own finances or those of his or her spouse or dependent children (see Section 82029 which defines "immediate family"). In addition, disqualification is required if the decision will affect any of several other economic interests, regardless of whether it will affect the official. Among those interests enumerated are a "source of income of \$250 or more" within the preceding 12-month

Richard E. Winnie
November 8, 1985
Page 3

period. To determine what constitutes a source of income, we must first turn to the Act's definition of income, which is found in Section 82030(a).

"Income" means, except as provided in subdivision (b), a payment received, including but not limited to any salary, wage, advance, dividend, interest, rent, proceeds from any sale, gift, including any gift of food or beverage, loan, forgiveness or payment of indebtedness received by the filer, reimbursement for expenses, per diem, or contribution to an insurance or pension program paid by any person other than an employer, and including any community property interest in income of a spouse. Income also includes an outstanding loan. Income of an individual also includes a pro rata share of any income of any business entity or trust in which the individual or spouse owns, directly, indirectly or beneficially, a 10-percent interest or greater. "Income," other than a gift, does not include income received from any source outside the jurisdiction and not doing business within the jurisdiction, not planning to do business within the jurisdiction, or not having done business within the jurisdiction during the two years prior to the time any statement or other action is required under this title.

Section 82030(a).

As can be seen, income of an individual also includes a pro rata share of income of any business entity in which the official owns a 10 percent interest or greater. When that pro rata share equals or exceeds \$250 in any 12-month period, the source of that income to the business entity becomes a "source of income" within the meaning of Section 87103(c), requiring disqualification as to decisions having a reasonably foreseeable material financial effect upon the source of income which is distinguishable from the effect on the public generally. Although the Commission's legal staff considers this to be a straight-forward statutory analysis, you have asked for reference to other legal authorities beyond the staff advice letters and Commission opinions previously sent to you.

Initially, reference is made to the Carey Opinion, 3 FPPC Opinions 99, No. 76-087, Nov. 3, 1977, which Ms. Donovan previously sent to you. Another copy is enclosed for your convenience in the event that you do not have the CEB publication of the Commission's Opinions. As can be seen from

Richard E. Winnie
November 8, 1985
Page 4

the Carey Opinion, it makes clear that a 10 percent or greater owner of a business entity receives pro rata income from customers of the entity. This interpretation is confirmed by the California Supreme Court's Opinion in Hays v. Wood (1979) 25 Cal. 3d 772; 160 Cal. Rptr. 102; 603 P.2d 19. That case dealt specifically with the disclosure of an attorney's clients because they were sources of income to his law practice. In considering the appropriateness of such a disclosure requirement, the court commented that the Act's disclosure scheme seeks "appropriate information about the sources and general magnitude of financial interests which may give rise to conflicts of interest...." (25 Cal. 3d at 782.) The court went on to state:

Unlike its predecessors, the current Act requires that disclosure of an official's income from business interests, when it exceeds a specified minimum, must include identification of the sources (e.g. customers and clients) from which the business entity itself received the income....

Viewing the source requirement ... we find no basis for concluding that such a requirement necessarily results in unwarranted and unconstitutional intrusion into protected zones of privacy. On the contrary, we believe that inquiry into actual sources bears a demonstrable relation to the substantial governmental interests here involved.... It is after all the clients or customers of a business entity in which a public official has a substantial interest who present the greatest potential source of conflicting obligations and interests....

... While the client or customer may not himself be in the public arena, his business or professional relationship with the official may well give rise to the opportunities for divided loyalties and a resulting potential for improper influence over the conduct of public affairs.

Hays v. Wood, Id. at 782-83.
(Emphasis added.)

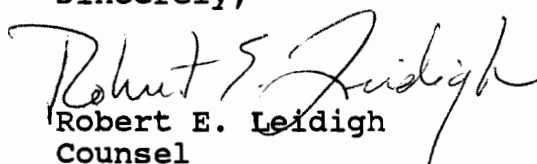
In addition to the foregoing legal authorities, you have received copies of numerous Commission advice letters which reiterate the Commission's position on this topic. I enclose

Richard E. Winnie
November 8, 1985
Page 5

for your benefit a copy of our most recent correspondence on the topic - an advice letter to Martinez City Councilman Peter Langley, No. A-85-216.

I hope that this letter provides further clarification of the legal authorities relied upon by the Commission for its long-standing position on this matter. Again, we would be pleased to meet with you, Mr. Lakey and Mr. Sproul to review your guidelines for councilmembers. We have agreed upon a meeting time of Monday, November 18, 1985, at 10:00 a.m. at the Commission's offices, 428 J Street, Sacramento, California, Eighth Floor. You will forward to me a copy of the guidelines so that we may review them in advance.

Sincerely,


Robert E. Leidigh
Counsel
Legal Division

REL:plh
Enclosures

F P P City of Oakland



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Office of the City Attorney

Richard E. Winnie

City Attorney

October 29, 1985

Barbara Milman, General Counsel
California Fair Political Practices Commission
428 J Street, Suite 800
P.O. Box 807
Sacramento, California 95814-0807

Re: Letter of October 7, 1985 from
Kathryn Donovan, FPPC

Dear Ms. Milman:

This letter is written in reference to a letter to me, dated October 7, 1985, from Kathryn Donovan, an attorney in the legal division of the Fair Political Practices Commission ("Commission"). The letter (a copy of which is enclosed) confirms telephone advice that she had provided to Assistant City Attorney Theodore R. Lakey regarding a possible conflict of interest situation involving an Oakland City Councilmember.

Initially, I wish to emphasize that the Office of the Oakland City Attorney has proceeded to advise the Councilmember in a manner consistent with Ms. Donovan's advice. Beyond the immediate situation, we are formulating guidelines of general application to assist City Councilmembers prospectively regarding how to identify and evaluate situations where a conflict of interest might arise.

The issue that Mr. Lakey discussed with Ms. Donovan was application of the Political Reform Act to situations where the only contact between the public official and the party that will benefit financially from a governmental decision is an attorney-client relationship. The situation posed by Mr. Lakey was the following:

1. It was reasonably foreseeable that the governmental decision would have a material financial effect on client's business, distinguishable from the effect on the public generally.
2. The councilmember's prorata share of the fees which the client had paid to the councilmember's law firm during the past twelve months was greater than \$250.
3. The councilmember's ownership interest in the law firm partnership was greater than ten percent.

4. The councilmember is not representing nor has he ever represented this client in connection with the transaction underlying the pending governmental decision.

When Mr. Lakey contacted your office his objective was to gain a clear understanding of legal authority related to this issue. He also sought information regarding the procedure and time required for obtaining an official opinion from the Commission. Ms. Donovan informed Mr. Lakey that a formal opinion would require at least forty-five days. Because the pending decision would be made in less than forty-five days, Mr. Lakey believed that he would be responsible for researching relevant law for advising the councilmember, utilizing whatever assistance the Commission could provide.

During all of our conversations, Ms. Donovan expressed the opinion that a conflict of interest would exist under the facts presented. Although she implied that her advice was consistent with previous opinions of the Commission involving similar circumstances, when we asked for citation to this authority Ms. Donovan merely directed Mr. Lakey to the relevant sections of the Act and Regulations and to the Thorner opinion (1 FPPC Opinions 198).

Because we found nothing in this authority that appeared to be directly on point, we retained the services of Curtis C. Sproul, an attorney with experience in this field, to obtain an independent evaluation of the matter. Pursuant to our instructions, Mr. Sproul contacted Ms. Donovan and determined that she was actually relying primarily upon informal advice letters from Commission staff. Mr. Sproul requested copies of these opinions from Ms. Donovan, since such opinions are not indexed in a manner that makes them easily accessible by the public. We received these informal advice letters on October 11, 1985.

It is not our objective to take issue with the conclusions reached by Ms. Donovan in this instance or by your office in past advice letters. Our single objective has been to gain a clear understanding of the basis for Ms. Donovan's conclusions so that we can properly advise our clients in this instance and in analogous future situations. Therefore, by this letter we express our concern with the difficulty which we have encountered in this case and to solicit your assistance for the future.

We do not feel that the legal basis for Ms. Donovan's advice is specifically addressed in the Act or Regulations or in any of the published opinions of the Commission. In defining an official's sources of income, this legal authority does not clearly contemplate a complete disregard of the business entity in which a public official owns a ten percent or greater interest under certain circumstances thereby creating a direct link between the official and a client of the official's business entity. The legal authority initially cited by Ms. Donovan could reasonably be interpreted to mean that only the business entity that is the official's direct source of income (in this case the councilmember's law firm) must meet the reasonably foreseeable material financial benefit tests of the regulations at Section 18702 of the Act before a prohibited conflict of interest is present.

Barbara Milman, Esq.
October 29, 1985
Page 3

With all due respect to the Commission's position on this matter as articulated in the informal advice letters, a different result could be reached by the following analysis:

Government Code Section 87100. No public official at any level of State or local government shall make, participate in making or in any way attempt to use his official position to influence a governmental decision in which he knows or has reason to know he has a financial interest.

Government Code Section 87103. An official has a financial interest in a decision within the meaning of Section 87100 if it is reasonably foreseeable that the decision will have a material financial effect, distinguishable from its effect on the public generally, on...(c) Any source of income,... aggregating \$250 or more in value provided to, received or promised to the public official within twelve months prior to the time when the decision is made.

For the purposes of defining the phrase "indirect investment or interest", the final paragraph of Section 87103 states that the phrase includes "a business entity...in which the official...owns directly, indirectly or beneficially a ten percent interest or greater". Interestingly the defined phrase does not appear in Section 87103 in connection with subparagraph (c) which is quoted above.

Government Code Section 82030. This section defines the income of an individual to include "a prorata share of any income of any business entity or trust in which the individual or spouse owns, directly, indirectly or beneficially, a ten percent interest or greater."

FPPC Regulation Section 18702(b) (3) states that, in determining whether it is reasonably foreseeable that the effect of a governmental decision will have a significant effect on a public official's source of income consideration should be given to whether:

(a) the effect of the decision will be to directly increase or decrease the amount of income to be received by the official "in an amount of \$100 or more"; or

(b) there is a nexus between the governmental decision and the purpose for which the official receives income; or

(c) in the case of the source of income that is a business entity, the business entity will be affected in a manner described in subsection (b)(1).

Regulations Section 18702(c) provides that the making or participating in the making of a governmental decision by a "person retained to provide... counsel has no material financial effect on a business entity or source of income in which such... person is retained as an officer, employee, sole proprietor or partner, if the only financial effects of the decision are the modification, perpetuation or renewal of the contractual or retainer agreement and/or the opportunity to bid competitively on the project or contract."

It is respectfully submitted that the above provisions, without the benefit of further regulations or published opinions, can be interpreted as saying that a conflict is present only when the official's source of income (in this case the law firm), itself, will be the potential beneficiary of a direct and material financial benefit in the magnitude defined in Reg §18702(b)(1) or when the decision will directly increase or decrease the official's income from the business or the business' income by \$100 or more. The sections cited above do not specifically require that the official's "business entity" be viewed as including the clients of the firm, particularly when the client has contracted with a party other than the official's in connection with the underlying transaction.

In addition to statutory and regulatory citations, Ms. Donovan suggested that we review the Tom Thorner FPPC opinion (1 FPPC Opinions 198). Although that opinion was instructive, its facts varied in several important respects from those presented in our situation. The facts in Thorner disclose that the official's own business, as opposed to a client of his business, stood to receive a material financial benefit from the governmental decision. The opinion also poses several hypothetical situations. In relation to the hypothetical situation most parallel to our own [subparagraph (c) found on pages 2 and 3 of the opinion], the Commission concluded that, based upon those facts, there may very well not be a conflict of interest (see pages 9 and 10 of the opinion).

Our independent analysis disclosed only one appellate court decision that appears to be parallel to our fact situation, namely the case of Witt vs. Morrow, 70 Cal.App.3d 817. In that case a San Diego City Councilmember appealed from an order enjoining him from participating in decisions concerning a shopping center project because of a conflict of interest. The councilmember was president of a non-profit corporation that owned a real estate interest that would benefit materially from approval of the shopping center project. He also served as attorney to the same non-profit corporation. The councilmember argued that, since he was paid a fixed monthly fee for his services as president of the corporation, decisions

Barbara Milman, Esq.
October 29, 1985
Page 5

regarding the shopping center project would have no material financial effect on his own finances. In rejecting these arguments, the court placed primary emphasis upon Morrow's the direct employment relationship with the non-profit corporation that stood to benefit from the decision. However, on page 823 the court made the following statement:

Morrow argues that BEE [the non-profit corporation] is not a "source of income" under the statute because this phrase refers only to himself and his business activity which produces the income and not the names of his customers or clients [citations omitted]. However, here Morrow characterizes his business activity as being an employee of BEE which is the source of this; if BEE were a client of his law firm then the source of this income would be Morrow's legal services." (Emphasis added).

Although the point that the court wished to make by the underlined statement is not exactly clear, it does suggest that a different result might have been obtained if the only relationship between Councilmember Morrow and BEE was that of attorney and client. The phrase can certainly be construed to mean that the court felt it might be appropriate to look no further than the law firm as Morrow's source of income, if his only relationship with BEE was that of attorney and client.

I have presented the above analysis, not to argue with Ms. Donovan's conclusions on the merits, but rather to indicate why our office believed that there was a legitimate need for identifying the legal authority upon which Ms. Donovan based her conclusions, before advice was rendered to the councilmember. When Ms. Donovan first spoke with us she did not mention the informal opinions that she later provided to us. These informal advice letters are far more directly on point than the official authority. I am advised that such informal opinions are not specifically indexed by topic and so it would be extremely difficult for local government officials to obtain the relevant opinions without assistance from your office.

We appreciate Ms. Donovan's assistance in gathering these informal opinion letters for our review. Unfortunately, we did not receive copies of these informal letters until two days before we received her October 7, 1985 letter. Interestingly, a copy of that letter was received by a representative of the press several days before it reached my office!

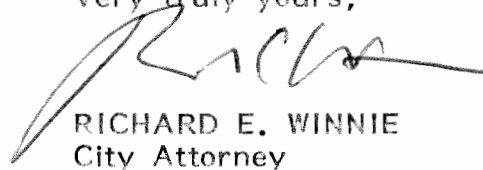
In reliance upon Ms. Donovan's informal advice, we have advised the councilmember to refrain from any participation in governmental decisions pertaining to the project at issue. He is following this advice. In order to provide general guidance to members of the City Council and other public officials that we represent, we are also drafting guidelines that can be used to provide early identification of potential conflicts of interest under similar circumstances in the future.

Barbara Milman, Esq.
October 29, 1985
Page 6

I would appreciate the opportunity to meet with you to review the guidelines which we are preparing and receive your comments on them. We are genuinely interested in developing a smooth working relationship with the Commission in order to avoid similar difficulties in the future and to develop lines of communication that are likely to facilitate a prompt review and consideration by your staff.

Later this week I will contact you to arrange a time when we can meet in Sacramento. Thank you in advance for your assistance in this matter.

Very truly yours,

A handwritten signature in dark ink, appearing to read 'R. Winnie', with a long horizontal flourish extending to the right.

RICHARD E. WINNIE
City Attorney

Attachment



California Fair Political Practices Commission

November 5, 1985

Richard E. Winnie
Oakland City Attorney
City Hall
One City Hall Plaza
Oakland, CA 94612

Re: A-85-228

Dear Mr. Winnie:

Your letter requesting advice under the Political Reform Act has been referred to Robert E. Leidigh, an attorney in the Legal Division of the Fair Political Practices Commission. If you have any questions about your advice request, you may contact this attorney directly at (916) 322-5901.

We try to answer all advice requests promptly. Therefore, unless your request poses particularly complex legal questions, or unless more information is needed to answer your request, you should expect a response within 21 working days.

Very truly yours,

Barbara A. Milman

Barbara A. Milman
General Counsel

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